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Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554

In Re:

Implementation of Sections of  
the Cable Television Consumer  
Protection and Competition Act  
of 1992

Rate Regulation

TO: The Commission

MM Docket ~~92-266~~

92-266

REPLY COMMENTS  
OF  
CORNING INCORPORATED AND SCIENTIFIC-ATLANTA, INC.

Richard E. Wiley  
Philip V. Permut  
Peter D. Ross  
Rosemary C. Harold  
WILEY, REIN & FIELDING  
1776 K Street, N.W.  
Washington, D.C. 20006  
(202) 429-7000

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In Re:

Implementation of Sections of  
the Cable Television Consumer  
Protection and Competition Act  
of 1992

Rate Regulation

MM Docket 93-215

TO: The Commission

REPLY COMMENTS  
OF  
CORNING INCORPORATED AND SCIENTIFIC-ATLANTA, INC.

Corning Incorporated ("Corning") and Scientific-Atlanta, Inc. ("Scientific-Atlanta"), by their attorneys, hereby submit their reply to comments on the Commission's proposed framework for cost-of-service regulation of cable rates.<sup>1</sup> Corning and Scientific-Atlanta submit that the records in this and the related benchmark proceeding strongly support adoption of the Commission's proposal for a streamlined mechanism for recovering the costs of cable system upgrades or rebuilds.<sup>2</sup> Indeed, the Commission's recent decision on reconsideration to disregard upgrade costs in its

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<sup>1</sup> Corning and Scientific-Atlanta also provide herein their comments on related issues raised in the Commission's Third Further Notice of Proposed Rulemaking in Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, FCC 93-428 (released August 27, 1993) ("Third NPRM") and, accordingly, request that this pleading be incorporated in that docket as well.

<sup>2</sup> See Notice of Proposed Rulemaking, MM Docket 93-215, FCC 93-353 (released July 16, 1993) ("Cost-of-Service NPRM") at ¶ 75.

benchmark approach has only underscored the necessity for a backstop -- short of a full cost-of-service proceeding -- to ensure continued capital investment in regulated cable service.<sup>3</sup>

The Commission, collectively and individually,<sup>4</sup> has continued to reaffirm its fundamental commitment to fashioning a rate regulation regime that -- as mandated by the Cable Television Consumer Protection and Competition Act of 1992 itself<sup>5</sup> -- recognizes rather than thwarts cable's vital role in our nation's communications infrastructure. As the NPRM in this proceeding stated:

[O]ur regulatory requirements for cost-based rates should also be designed to assure that cable operators may fully respond to incentives to provide a modern communications infrastructure and to respond to competitive forces.<sup>6</sup>

Moreover, the 1992 Cable Act not only endorses this objective, but also specifically mandates that the Commission's regulation of cable rates take due account of the costs of providing regulated

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<sup>3</sup> See First Order on Reconsideration, MM Docket No. 92-266, FCC 93-428 (released August 27, 1993) ("Reconsideration Order").

<sup>4</sup> See Corning and Scientific-Atlanta Reply to Oppositions to Petition for Reconsideration in MM Docket No. 92-266 (filed August 4, 1993) ("Corning/Scientific-Atlanta Reply") at 5-6.

<sup>5</sup> Pub. L. No. 102-385, 106 Stat. 1460 (1992) ("1992 Cable Act").

<sup>6</sup> Cost-of-Service NPRM at ¶ 9; see also Corning/Scientific-Atlanta Reply at 2-3.

cable service.<sup>7</sup> Yet after initial construction, capital investment for system expansion and upgrades is likely to be the single largest cost a cable operator directly incurs.<sup>8</sup> Thus, as Corning and Scientific Atlanta have previously demonstrated,<sup>9</sup> the Commission's rate regulations would not only contravene this mandate but also seriously retard the rapidly growing rate of advanced technology deployment if they fail to provide cable operators the means to recover readily, and earn a reasonable return on, capital investments.

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<sup>7</sup> See 47 U.S.C. § 543(b)(2)(c), 543(c)(2)(E).

<sup>8</sup> The necessity and magnitude of this investment has only become greater, moreover, in the face of the Cable Act's "must-carry" and consumer equipment compatibility obligations, as well as the impending transition to advanced television.

Despite the subsequent cost savings typically produced by the deployment of optical fiber and related advanced technology, cable operators simply cannot absorb the substantial upfront capital outlays necessary for system upgrades to improve regulated service without adequate cash flow or available financing. See Petition for Reconsideration of Corning and Scientific-Atlanta in MM Docket No. 92-266 (filed June 21, 1993) ("Corning/Scientific-Atlanta Petition") at 8-14. Thus, the suggestion of some commenters that any cost savings or revenue increases from such system improvements should be offset against the investment recoverable under rate regulation is not only flatly inconsistent with cost-of-service, but also -- by denying the benefit of both lower costs and higher revenues -- would leave cable operators with simply no economic incentive to invest in system improvements. See, e.g., Comments of BellSouth Telecommunications, Inc. in MM Docket No. 93-215 (filed August 25, 1993) at 31.

<sup>9</sup> See Corning/Scientific-Atlanta Petition at 5-14, 18-20.

The Commission has confirmed that it has no intention of allowing these critical costs to go unrecovered.<sup>10</sup> Despite its general desire to rely on the benchmark/price cap mechanism as its primary tool for cable rate regulation, however, the Commission for now has delegated to its cost-of-service standards the primary duty to ensure cable operators the ability to recover the costs of their capital investment.<sup>11</sup>

The benchmark/price cap mechanism, as tentatively explicated in the Commission's Third NPRM,<sup>12</sup> would still typically fail to permit the full recovery of capital investment in upgrades and rebuilds. The substantial evidence (presented in MM Docket No. 92-266) demonstrating this effect of a sharply reduced marginal benchmark rate remains unrefuted,<sup>13</sup> notwithstanding some commenters' bald assertions to the contrary.<sup>14</sup> Furthermore, the

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<sup>10</sup> See Third NPRM at ¶ 136.

<sup>11</sup> See Reconsideration Order at ¶ 97.

<sup>12</sup> See Third NPRM at ¶¶ 136-143.

<sup>13</sup> If the Commission were instead to allow the benchmark adjustment to incorporate, at least in part, the system's preexisting marginal benchmark rate, it would mitigate the otherwise significant shortfall in cash flow necessary to support an upgrade.

<sup>14</sup> No party has challenged, for example, the Deloitte & Touche analysis demonstrating that capital investment is in fact the most likely victim of the benchmark/price cap mechanism's squeeze on cash flow, which is of course the determinant of both system revenues and access to capital. See Deloitte & Touche, Estimated Impact of Cable Rate Regulation on Cable Television Cash Flows and Capital Expenditures (June 1993) at 4-6, appended to

benchmark/price cap mechanism's failure to account for the massive capital expenditures inherent in system upgrades or expansions would not be cured by the Commission's current proposal to incorporate within the benchmark the programming costs of filling added channel capacity.<sup>15</sup> In light of this suggested approach to benchmark adjustments, the Commission's proposed streamlined cost-of-service mechanism would appear to offer the only means by which the Commission can spare regulators and cable operators alike the burden of full cost-of-service proceedings every time an operator wishes to rebuild or upgrade its system.<sup>16</sup>

As the Commission explained in its Reconsideration Order, the external treatment of capital investment could effectively be accomplished by an add-on to the benchmark/price cap rate to cover the costs of an upgrade for regulated cable service -- much like

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<sup>14</sup>(...continued)  
Corning/Scientific-Atlanta Petition. See also J. Dertouzos & S. Wildman, Regulatory Benchmarks for Cable Rates: A Review of the FCC Methodology (June 21, 1993) at 8, appended to Petition for Reconsideration and Clarification of Viacom International Inc., MM Docket No. 92-266 (filed June 21, 1993); and Joint Letter of Commercial Banks, MM Docket 92-266 (filed June 21, 1993).

<sup>15</sup> Indeed, given that investment in expanding channel capacity is generally a prerequisite to programming additions, the cost of additional programming services will never come to pass if cable operators are unable first to undertake and successfully complete a cost-of-service showing.

<sup>16</sup> This proposal to allow for benchmark recovery of the programming costs attending an expansion in system capacity would nonetheless serve as an appropriate complement to the Commission's proposal for streamlined upgrade cost showings.

the proposed treatment of added programming services, but reviewed on a streamlined cost-of-service basis.<sup>17</sup> Indeed, even beyond the cable industry support for some mechanism short of a full cost-of-service showing for recovery of these costs, local and state authorities have also cited upgrade costs as singularly appropriate for streamlined treatment within the Commission's overall cost-of-service standards.<sup>18</sup>

This add-on approach would, as the Commission appropriately contemplates, permit an operator to increase its per-channel rate to the extent necessary to finance the otherwise unrecovered costs of system improvements for regulated cable service.<sup>19</sup> The add-on could be calculated based on the incremental cash flow necessary to support the upgrade, accounting for plant under construction, depreciation, increased maintenance and operating expenses, added programming expenses (if not already covered in a benchmark adjustment), and the cost of capital to finance the investment,

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<sup>17</sup> See Reconsideration Order at ¶ 97.

<sup>18</sup> See, e.g., Comments of Utah League of Cities and Towns at 7; see also Comments of National Association of Telecommunication Officers and Advisors ("NATOA"), et al. at 15.

<sup>19</sup> No one has refuted the substantial benefits of signal quality, system reliability, and channel capacity that optical fiber and related advanced technologies afford to the subscribers of regulated cable service. Moreover, the Commission has made clear its intent to resolve in this proceeding the allocation and other routine questions inherent in rate regulation, and those determinations would likewise govern this streamlined showing of upgrade costs.

including a reasonable rate of return. When seeking to raise rates on this basis, the cable operator would be obligated to present its underlying calculations and rationale to the reviewing body upon request.<sup>20</sup>

As the Commission suggests in its Reconsideration Order, this streamlined cost-of-service showing for the costs of upgrades or rebuilds could easily evolve over time into a more formulaic -- and thus even more administratively efficient -- "benchmark-plus" approach.<sup>21</sup> The Commission's announced cost studies, ultimately supplemented by early cost-of-service showings, will provide the Commission with authoritative data from which it could establish an appropriate range of upgrade costs automatically permitted under this add-on formula.

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<sup>20</sup> Corning and Scientific-Atlanta fully agree with the Commission's general comments regarding the appropriateness and consistency of allowing external treatment for the costs of franchise-required upgrades. See Reconsideration Order at n. 160; see also Third NPRM at ¶¶ 153-54. The calculation of those costs should generally follow the approach described above, which will take its final shape from the cost-of-service standards ultimately adopted by the Commission. It would be inconsistent and unsound as a matter of policy, however, to grant local franchise authorities broad discretion in setting the standards for cost-of-service showings or even second-guessing the appropriateness of upgrades not required by the franchise. Longstanding federal policy has recognized the overriding national interest in the development of advanced telecommunications infrastructure. This vital federal interest could be effectively thwarted by a patchwork of inconsistent local determinations rendered by franchise authorities controlling cable operator's ability to recover their capital investments.

<sup>21</sup> See Third NPRM at n. 259.



In sum, the record before the Commission provides ample support for supplementing its benchmark/price cap approach with a streamlined cost-of-service mechanism to ensure cable operators recovery of the capital investments necessary to improve regulated cable service. Failure to provide such full recovery will either compel widespread reliance on full cost-of-service showings or, worse yet, stifle cable investment.

Respectfully submitted,

CORNING INCORPORATED  
SCIENTIFIC-ATLANTA, INC.

By: 

Richard E. Wiley

Philip V. Permut

Peter D. Ross

Rosemary C. Harold

of

WILEY, REIN & FIELDING

1776 K Street, N.W.

Washington, D.C. 20006

(202) 429-7000

Their Attorneys

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